LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS

200 W. Washington, Suite 301
Indianapolis, IN 46204
(317) 233-0696
http://www.in.gov/legislative

FISCAL IMPACT STATEMENT

LS 7582 | **NOTE PREPARED:** Jan 13, 2003
BILL NUMBER: SB 386 | **BILL AMENDED:**

SUBJECT: Venture Capital Investment Tax Credit.

FIRST AUTHOR: Sen. Kenley | **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: <u>**X**</u> **GENERAL** | **IMPACT:** State
<u>**X**</u> **DEDICATED**
FEDERAL

<u>Summary of Legislation:</u> The bill specifies that a pass through entity is eligible for the Venture Capital Investment Tax Credit for investments made in qualified Indiana businesses. The bill eliminates certain requirements that a business must meet in order to be certified as a qualified Indiana business. The bill specifies that the total credit amount calculated for a qualifying taxpayer for a particular taxable year counts toward the $10,000,000 in maximum allowable credits for that calendar year, regardless of whether the taxpayer's total credit amount exceeds the taxpayer's tax liability and may be carried over to the succeeding year. The bill provides that if a taxpayer carries over any credit amount to the succeeding year, the amount carried over does not count toward the $10,000,000 in maximum allowable credits for the succeeding year. The bill allows the Department of Commerce to adopt rules to limit the number of succeeding taxable years over which an unused credit may be carried forward. It provides that if the Department adopts such rules, any unused credit amount remaining at the end of the allowable carry-forward period becomes available for eligible taxpayers in the next calendar year and is added to the $10,000,000 in maximum allowable credits for that next calendar year. The bill also provides that if a taxpayer files a return claiming a credit after the maximum amount of allowable credits has been allocated for the calendar year, the department of state revenue may, at the request of the filer, approve the claimed credit with respect to the next calendar year.

<u>Effective Date:</u> January 1, 2003 (retroactive).

<u>Explanation of State Expenditures:</u>

<u>Explanation of State Revenues:</u> The bill makes changes to the Venture Capital Investment Tax Credit that could potentially increase the annual total credits claimed above the existing statutory limit of $10 M in tax years 2005 to 2008. While this would not affect revenues in FY 2004, it could potentially reduce revenue by more than $10 M in FY 2005. This would be contingent on the amount of carryover credits and new credits that taxpayers are able to claim in tax year 2005. The bill also could potentially expand the pool of taxpayers that qualify for the tax credit. The revenue loss due to this change is indeterminable.

Background: Under the Venture Capital Investment Tax Credit, a taxpayer is entitled to a nonrefundable tax credit equal to the lesser of: (1) 20% of qualified investment capital (debt or equity capital) provided to a *qualified Indiana business* during a calendar year; or (2) $500,000. The tax credit is allowed for venture capital investment made from January 1, 2004 to December 31, 2008. In addition, current law limits to $10 M the total tax credits that may be claimed in calendar year. Under current law, a taxpayer may claim the credit against the State Gross Retail and Use Tax, Adjusted Gross Income (AGI) Tax, Financial Institutions Tax, or Insurance Premiums Tax liability. While the tax credit is nonrefundable, it may be carried forward to subsequent years. No carryback of the tax credit is allowed. If a pass through entity does not have a tax liability, the credit may be taken by shareholders, partners, or members in proportion to their distributive income from the pass through entity. Under current law, the Indiana Department of Commerce (IDOC) must certify whether a business is a *qualified* Indiana business for purposes of obtaining venture capital investment that qualifies for the tax credit. The IDOC must certify a business as qualified if it meets the following criteria:

(1) it is a high growth company that is entering a new product or process area, has a substantial number of college educated or high skill employees, and has substantial number of employees earning at least 150% of Indiana per capita personal income;

(2) it has its headquarters in Indiana;

(3) it is primarily focused on research and development, technology transfers, or the application of new technology, or has significant potential of bringing substantial capital into Indiana, creating jobs, or diversifying the business base in Indiana;

(4) it has had average annual revenue less than $10 M in the two preceding years;

(5) at least 50% of its employees reside in Indiana and at least 75% of its assets are located in Indiana; and

(6) it is not engaged in one of six specified businesses.

The bill provides that the $10 M annual limit on total credits allowed applies only to the new credits approved for venture capital provided during that year. In addition, all new credits approved during the year would count toward the $10 M maximum regardless of whether the new credits are used entirely or carried over to subsequent taxable years by the taxpayer. Thus, carryover credits claimed in a taxable year are not counted toward the $10 M annual maximum. This means that the combined total of new credits and carryover credits claimed against tax liabilities could exceed $10 M beginning in tax year 2005. It is important to note that the bill also would allow the IDOC to limit the years over which tax credits may be carried over. If such a limit is imposed by the IDOC, the bill requires that tax credits that are not exhausted by a taxpayer at the end of the carryover period must be added to the $10 M limit for new credits in the following year. The impact of this provision is contingent on IDOC action to establish a limited carryover period.

The bill also makes changes to the criteria for certifying a business as a qualified Indiana business for venture capital investment that may be claimed by the investor under the Venture Capital Investment Tax Credit.

These changes could potentially increase the number of businesses in which creditable venture capital investment may be made. Under the bill, the certification criteria described in (1) above is eliminated. Also, under the bill, a business would no longer have to meet both the employee and asset requirements described in (5) above. The business would only have to meet one of these requirements.

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue, Indiana Department of Commerce.

Local Agencies Affected:

Information Sources:

Fiscal Analyst: Jim Landers, 317-232-9869